

Texas Commission on Environmental Quality

Interoffice Memorandum

To: Commissioners **Date:** February 17, 2017

Thru: Bridget C. Bohac, Chief Clerk
Richard A. Hyde, P.E., Executive Director

From: Steve Hagle, P.E., Deputy Director
Office of Air

Docket No.: 2016-1429-RUL

Subject: Commission Approval for Proposed Rulemaking
Chapter 101, General Air Quality Rules
Emissions Banking and Trading Revisions for Area and Mobile Source
Credit Generation
Rule Project No. 2016-041-101-AI

Background and reason(s) for the rulemaking:

This rulemaking would revise two divisions of emissions banking and trading (EBT) rules in 30 Texas Administrative Code (TAC) Chapter 101, Subchapter H, which define several market-based programs that provide sites with additional flexibility for complying with air regulations. In 1993, the Texas Commission on Environmental Quality (TCEQ), or commission, adopted the Emission Credit Banking and Trading rules in Chapter 101, Subchapter H, Division 1 to allow sources in nonattainment areas to generate, bank, trade, and use credits from permanent reductions in emissions. In 1997, the TCEQ adopted the Discrete Emission Credit Banking and Trading rules in Chapter 101, Subchapter H, Division 4 to allow sources statewide to generate, bank, trade, and use credits from reductions in emissions below regulatory requirements.

The current EBT rules allow an area or mobile source to generate emission credits from emissions reductions that are demonstrated to be real, quantifiable, permanent, enforceable, and surplus to the state implantation plan (SIP) and all applicable rules, and discrete emission credits from reductions that are real, quantifiable, and surplus to the SIP and all applicable rules. However, research into the feasibility of generating area and mobile source credits uncovered significant implementation issues associated with ensuring that area and mobile source credits meet the United States Environmental Protection Agency (EPA) and Federal Clean Air Act (FCAA) requirements.

Below are some of the implementation issues for generating credits from area and mobile sources.

Real and Surplus

- Accounting for the potential uncertainty associated with verifying the SIP emissions for an individual source given that current non-point emissions inventory estimation techniques do not quantify emissions on a source-level basis.
- Accounting for the mobile source fleet turnover assumptions used in the SIP.
- Ensuring actual emissions are reduced and that those reductions are enforceable through existing agency processes.

Re: Docket No. 2016-1429-RUL

- Accounting for the potential overall increase in nonattainment area emissions from shifting activity within the same nonattainment area to meet market demand vacated by the source that generated the credits.

Quantifiable

- Accounting for uncertainty in emission calculation techniques since emissions monitoring, testing, and recordkeeping requirements typically differ significantly for area and mobile sources versus point sources.

Permanent and Enforceable

- Ensuring that the emissions reduction implemented to generate an area and mobile source credit is permanent and unchanging for the remaining life of the facility or mobile source.

At the December 10, 2014 agenda, based on the identified implementation issues, the commission had proposed to remove the provisions for generating credits from area and mobile sources. The commission subsequently received significant public comment opposing the removal of these area and mobile source credit provisions. Therefore, at the June 3, 2015 agenda the commission retained the rules that allow an area or mobile source to generate credits, although the commission did emphasize that significant issues remain with generating credits from area and mobile sources in a manner consistent with federal requirements. In addition, the commission directed staff to identify potential viable options for generating credits from area and mobile sources or bring the issue back before them for potential removal. The commission also indicated that interested parties should engage with staff to discuss issues and potential options that would help to make retaining the area and mobile source generation of credits feasible. In meeting the commission's direction, staff has worked with external parties, including the EPA, to identify a viable option for limited area and mobile sources.

The proposed rulemaking would amend Chapter 101, Subchapter H, Division 1 and Division 4, to address the issues identified with area and mobile source credit generation and use. If adopted, the revisions will be submitted to the EPA as a revision to the SIP.

Scope of the rulemaking:

The proposed rulemaking would amend the following sections of Chapter 101, Subchapter H.

- Division 1, §§101.300, 101.302 - 101.304, and 101.306; and
- Division 4, §§101.370, 101.372 - 101.374, and 101.376.

Generally, the proposed rules specify the requirements for owners of area and mobile sources to generate emission credits. While this opportunity theoretically exists under current rule language, it has rarely been feasible. In addition to expanding the opportunity for area and mobile sources to generate credits, the proposed rulemaking also includes changes that make the requirements for the use of emission credits from mobile sources consistent with the use of credits from stationary sources.

Re: Docket No. 2016-1429-RUL

A.) Summary of what the rulemaking will do:

The proposed rulemaking would:

- Limit the types of area and mobile sources that are eligible to generate credits to help ensure that the process is feasible and the reductions are real and surplus by prohibiting credit generation from:
 - individual area source facilities and mobile sources that did not operate during the latest National Emissions Inventory (NEI) year related to the applicable SIP revision;
 - individual facilities and mobile sources that cannot generate at least 0.1 ton of credit after all required adjustments are applied;
 - sources without records documenting approved or approvable methods to quantify emissions;
 - residential area sources;
 - the shutdown of area source types that are formally identified on the TCEQ's website, after an opportunity for public comment, as being inelastic, highly interchangeable, and driven by population needs (such as gas stations, dry cleaners, restaurants, and concrete batch plants);
 - the shutdown or replacement of a mobile source unless that source is rendered permanently inoperable or removed from North America;
 - on-road mobile sources that are not part of an industrial, commercial, nonprofit, institutional, or municipal/government fleet; and
 - most mobile sources that do not operate predominantly within the nonattainment area.
- Reduce the eligible SIP emissions for credit generation projects to mitigate any uncertainties associated with the limited use of source-specific data to determine SIP emissions for the area, on-road mobile, or non-road mobile source categories.
- Revise the definition of SIP emissions to specify that, for area and mobile sources, credits will only be generated for actual emissions and that credits will not be issued beyond the amount of actual emissions during the latest NEI year related to the applicable SIP, not to exceed any applicable local, state, or federal requirement.
- Allow that the year used to determine SIP emissions be specifically identified by the commission in SIP revisions adopted after December 31, 2017.
- Extend the deadline for applying to generate credits from mobile sources to be consistent with the deadline for generating credits from area and point sources.
- Define the years used to determine the historical adjusted emissions (or "lookback" for setting baseline emissions) for area and mobile sources.
- Specify the procedure for reducing the amount of credits issued for an individual mobile source based on its remaining useful life to ensure the credits are surplus to the fleet turnover assumptions used in the SIP and annualizing the credits generated to account for use at a point source.
- Reduce the amount of credits issued for the shutdown of an individual area source to account for the potential overall increase in nonattainment area emissions from shifting activity.

Re: Docket No. 2016-1429-RUL

- Reduce the amount of credits issued for an individual source based on the quality of the data used to determine the emissions.
- Provide additional means to specify monitoring, testing, recordkeeping, and reporting requirements and to make the emissions reduction permanent and federally enforceable.
- Require verification that a replaced or shutdown mobile source is rendered permanently inoperable or removed from North America.
- For area and mobile sources, require the submission of a certification making the emissions reduction and any associated monitoring, testing, or recordkeeping requirements permanent and federally enforceable.
- Require the owner or operator of a facility subject to the requirements of 30 TAC Chapter 106, concerning Permits by Rule, or a permit issued under 30 TAC Chapter 116, concerning Control of Air Pollution by Permits for New Construction or Modification, to use the relevant testing and monitoring methodologies in these chapters to show compliance if the facility is not otherwise subject to an EPA-approved rule with testing and monitoring requirements, such as Chapter 117.
- Require credit applications to be submitted through the State of Texas Environmental Reporting System (STEERS) unless the applicant receives prior approval for an alternative form of application submission.
- Provide potential applicants more flexibility regarding the use of emission credits, such as expanding the ability to use credits for interpollutant trades, and the timeline for submitting credit generation applications in certain circumstances.
- Establish a temporary extension of the application and credit use deadlines to improve the viability of credit generation for applicants potentially influenced by deferred application processing during this rulemaking.
- Establish an extension to the credit application and credit life as an incentive for emission credit generation from oil and gas production sites that expeditiously plug wells.

In addition, staff recommends making non-substantive revisions to remove or revise obsolete and redundant language, use consistent terminology, and update the rule language to current *Texas Register* and TCEQ style and format requirements.

B.) Scope required by federal regulations or state statutes:

None of the changes are required by federal rules or state statutes.

C.) Additional staff recommendations that are not required by federal rule or state statute:

All the revisions are staff recommendations based on stakeholder comments received. The substantive revisions are described above.

Statutory authority:

The rulemaking is proposed under Texas Water Code (TWC), §5.102, concerning General Powers, TWC, §5.103, concerning Rules, and TWC, §5.105, concerning General Policy, that authorize the commission to adopt rules necessary to carry out its powers and duties under the TWC; and under Texas Health and Safety Code (THSC), §382.017, concerning

Re: Docket No. 2016-1429-RUL

Rules, that authorizes the commission to adopt rules consistent with the policy and purposes of the Texas Clean Air Act. The rulemaking is proposed under THSC, §382.002, concerning Policy and Purpose, that establishes the commission's purpose to safeguard the state air resources, consistent with the protection of public health, general welfare, and physical property; THSC, §382.011, concerning General Powers and Duties, that authorizes the commission to control the quality of the state's air; THSC, §382.012, concerning State Air Control Plan, that authorizes the commission to prepare and develop a general, comprehensive plan for the control of the state's air; THSC, §382.014, concerning Emission Inventory, that authorizes the commission to require a person whose activities cause air contaminant emissions to submit information to enable the commission to develop an emissions inventory; THSC, §382.016, concerning Monitoring Requirements; Examination of Records, that authorizes the commission to prescribe requirements for owners or operators of sources to make and maintain records of emissions measurements; and THSC, §382.021, concerning Sampling Methods and Procedures, that authorizes the commission to prescribe the sampling methods and procedures to determine compliance with its rules. The amended sections are also proposed under THSC, §382.023, concerning Orders, and §382.036, concerning Cooperation and Assistance. The rulemaking is also proposed under FCAA, 42 United States Code, §§7401, *et seq.*, which requires states to submit SIP revisions that specify the manner in which the National Ambient Air Quality Standard will be achieved and maintained within each air quality control region of the state.

The proposed amendments implement THSC, §§382.002, 382.011, 382.012, 382.014, 382.016, 382.017, 382.021, 382.023, and 382.036.

Effect on the:

A.) Regulated community:

The rule amendments would increase flexibility of the programs overall but make some provisions more protective and legally sound, such as specifically disallowing credit generation from area and mobile sources that cannot meet all programmatic requirements. The provisions for area and mobile sources would remain in the rules and qualified sources that meet all programmatic requirements may generate credits.

B.) Public:

The proposed revisions should increase the utility of the EBT programs for area and mobile sources, which could result in increased benefits to air quality and provide economic benefits in the nonattainment areas.

C.) Agency programs:

There will be increased workload for the Air Quality Division from reviewing area and mobile source credit generation applications and for the Air Permits Division to process air authorizations anticipated to be amended or reviewed from permitted or registered facilities to meet the enforceability requirement. The workload increase estimate is based on the assumption that approximately 100 additional applications will be received per year. The EBT Program has historically processed primarily point source applications, and addition of processing credit applications from area and mobile sources is expected to

Re: Docket No. 2016-1429-RUL

increase the workload by one third to one half. However, it is difficult to anticipate the number or complexity of applications that will be voluntarily submitted.

The responsibilities associated with credit applications include:

- reviewing applications for regulatory requirements and ensuring no SIP issues;
- calculating the potential credits;
- interacting with applicants to gather the necessary information to fully assess the application;
- entering information in database for trades and tracking;
- issuing certifications to make credited emissions reductions permanent and enforceable;
- processing changes to existing permit authorizations for new emission limits associated with credit applications;
- processing permit by rule applications for new emission limits associated with credit applications; and
- maintaining the ePermits program for certifications submitted for area source applications.

Stakeholder meetings:

Six open-participation stakeholder meetings were held in Houston, Arlington, and Austin between July 20 to 25 and December 6 to 9, 2016. The initial concepts for the rulemaking were discussed and stakeholder input was requested, especially on examples of how credits could be generated by area and mobile sources. Attendees from industry, citizen's groups, government, and consulting firms participated. In the month after the July meetings, stakeholders (including several who did not attend a meeting) provided comments and suggestions for rule changes. Different stakeholders suggested various potential changes, some of which are included in the revisions. Most of the stakeholders who commented were opposed to adjusting the quantity of credits from area and mobile sources based on the quality of data used to estimate emissions, reducing the quantity of SIP emissions that could be credited, and limiting the "lookback" for area and mobile sources to less than ten years (as it is for point sources). The proposed rules were drafted with stakeholder input taken into account, however, the need to meet EPA and FCAA requirements is in conflict with some stakeholder suggestions.

Potential controversial concerns and legislative interest:

Historically, there has been legislative interest in increasing the flexibility of credit generation, but no specific legislative interest has been expressed concerning these proposed rule revisions. This rulemaking attempts to address the significant regulatory and financial responsibility associated with implementing a credit generation program for area and mobile sources that is consistent with federal requirements. As such, one concern with the proposal is the possible risk of the EPA not approving the provisions. Specifically, the EPA has expressed concern that the rulemaking ensure the credits from area and mobile sources can be proven to meet the federal requirements related to the credited emissions reductions being surplus, real, quantifiable, enforceable, and permanent. The regulated community has expressed concern regarding the limitations on the total quantity of creditable emissions, the potential reduction in credits issued based

Re: Docket No. 2016-1429-RUL

on the quality of data used for emission estimation, and the requirement that mobile sources used to generate credits be made permanently inoperable or removed from North America.

Will this rulemaking affect any current policies or require development of new policies?

The rulemaking incorporates existing guidance for the inter-pollutant use of credits into the rules for credits generated by mobile sources but has no impact on any existing policies. Changes to the database for the program will need to be made to be consistent with the rule changes.

What are the consequences if this rulemaking does not go forward? Are there alternatives to rulemaking?

This rulemaking is not required by federal regulation or state statute, so the changes are not mandatory. However, the changes should make the area and mobile source aspect of the existing EBT credit generation programs a practical option, which could result in more credits being generated and provide economic benefits in the nonattainment areas.

Key points in the proposal rulemaking schedule:

Anticipated proposal date: March, 8, 2017

Anticipated *Texas Register* publication date: March 24, 2017

Anticipated public hearing date (if any): April 18 - April 20, 2017

Anticipated public comment period: March 24, 2017 - April 24, 2017

Anticipated adoption date: August 2017

Agency contacts:

Guy Hoffman, Rule Project Manager, Air Quality Division, (512) 239-1981

Amy Browning, Staff Attorney, (512) 239-0891

Derek Baxter, Texas Register Rule/Agenda Coordinator, (512) 239-2613

Attachments:

None

cc: Chief Clerk, 2 copies
Executive Director's Office
Marshall Coover
Erin Chancellor
Stephen Tatum
Jim Rizk
Office of General Counsel
Guy Hoffman
Derek Baxter